

Opening Statement
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Chairman
Permanent Subcommittee on Investigations
Hearing On
GSA Contractors Who Cheat on Their Taxes
And What Should Be Done About It
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Good morning and welcome to today's hearing. This is the third Subcommittee hearing focusing on federal contractors with unpaid tax debts. These are not your everyday tax delinquents, but rather contractors who receive millions of dollars from American taxpayers and yet refuse to pay their fair share of taxes.

Some of these tax-delinquent contractors fraudulently used withheld payroll taxes for their business or personal use. Keep in mind that payroll taxes include withholdings from employees' wages for Social Security, Medicare, and individual income taxes. These contractors, like all employers, hold these wages in trust for their employees and are required to remit them to the IRS. Rather than fulfilling their legal obligations, these contractors have diverted the money for their own personal gain. An investigation by the Government Accountability Office in conjunction with this Subcommittee uncovered numerous contractors who bought luxury cars, boats, and multi-million dollar properties, even though they owed hundreds of thousands of dollars in unpaid taxes.

To get a sense of the problem, let's review of handful of disturbing cases:

- One contractor that provides security services for the federal government was paid more than \$1 million from the American taxpayers over the past two years, even though he owes more than \$12 million in payroll taxes. Over the last few years, as his company failed to turn over payroll taxes it withheld from its employees paychecks, the owner made large cash withdrawals from the company for his personal use. More than \$100,000 of that money was spent gambling.
- Another contractor who provides public communications services to the federal government was paid \$100,000 and owes more than \$2 million in payroll taxes. While he kept his employees' payroll taxes, the owner purchased a residential property valued at \$1 million, and made numerous cash withdrawals totaling \$500,000 at casinos.
- A third contractor who sells emergency supplies was paid \$100,000 by the federal government, while simultaneously owing more than \$700,000 in back taxes. The IRS assessed a penalty against the owner for failing to remit payroll taxes and imposed a

federal tax lien that was in effect when the contractor received a federal contract. While refusing to pay his employees' payroll taxes, the owner made several real estate purchases, including a million dollar home.

Sadly, these are just the tip of the iceberg. The Subcommittee's efforts – in concert with the hard work of Government Accountability Office – have revealed that **3,800** federal contractors who contract with the General Services Administration owe back taxes amounting to **a \$1.4 billion**. In an age of increasingly tight fiscal discipline, that \$1.4 billion could be put towards our homeland security, our children's education, or job training programs. It adds insult to injury that these tax deadbeats are actually paid enormous amounts of money every year from American tax coffers.

Our hearing today will address why these tax cheats were able to do business with the government in the first place, and what we need to do to put a stop to it. This hearing continues our long-standing investigation of federal contractors who cheat on their taxes. In February 2004, the Subcommittee held a hearing that examined federal contractors doing business with the Department of Defense who owed \$3 billion in unpaid taxes. In June 2005, the Subcommittee held a hearing that identified \$3.3 billion dollars in unpaid taxes by civilian contractors at various federal civilian agencies. This third hearing will focus on GSA contractors who provide a vast array of products and services to the federal government, ranging from office supplies, furniture, communications equipment, security services, automobiles, office space and landscaping. We will also explore how to fix the problem so that these contractors cannot continue fleecing the American taxpayers.

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There is an old adage that states: "If you want the right answer, you have to ask the right question." When it comes to federal contractors, we have been asking the wrong questions. The federal government has been trying since 2000 to identify tax cheats by asking federal contractors one narrow question – whether they have been indicted for or convicted of tax evasion in the last three years. The Subcommittee's investigation has shown, however, that this question is simply too narrow to weed out tax-delinquent contractors. The simple fact is that not all tax frauds result in a conviction for tax evasion. Indeed, there is a broad spectrum of tax-related violations that are utterly ignored by our contracting review process. As a result, many federal contractors continue to receive contracts even though they owe a massive amount in back taxes.

Take the case of Jack Easterday, who is the owner of nine nursing homes and a computer software firm in California. Just a few weeks ago, Mr. Easterday was convicted on 47 counts of failing to turn over as much as \$3 million in payroll taxes that he had withheld in trust for his employees. He used the money for personal gain. He paid himself and his wife an average annual salary of more than \$338,000 between 1998 and 2004. He purchased a 10,000 square foot home for \$750,000 in 1997. He purchased a dining room table and chairs that seated 22 people along with a 24 place setting of Limoges china. He purchased a Rolex watch for \$16,340. He owned a sailboat and jet skis. He was living like Louis XIV, compliments of the American taxpayer.

Mr. Easterday was convicted of willfully failing to account for and turn over payroll taxes. More importantly, he was not convicted of tax evasion, which is a different violation of the code. Consequently, Mr. Easterday can honestly represent that he has not been indicted for or convicted of tax evasion in the last three years, and therefore, he would remain eligible to contract with the federal government in the future.

Mr. Easterday is just one of the 97 known cases of egregious tax abuse by federal contractors that were identified by the Subcommittee, with the assistance of GAO. These 97 contractors are the worst of the worst. Yet, none of those 97 contractors has been indicted for or convicted of tax evasion. Therefore, every single one of those “worst of the worst” would be able to slip their tax violations by our contracting personnel. On the other hand, if we had asked those 97 contractors, including Mr. Easterday, the right questions, we would have known that they were tax deadbeats before we gave them contracts. Clearly, we are asking the wrong questions.

But that is only half of the problem. The other half is that there is no verification of the tax-related representations that contractors make. Even when we ask contractors if they have been indicted for or convicted of tax evasion, we do not identify those who lie. Neither the Internal Revenue Service nor the Department of Justice currently provides GSA with lists of persons or companies who have been indicted for or convicted of tax evasion. Therefore, GSA has no method to verify whether contractors’ representations are true. Clearly, we must not only ask the right questions, but also verify the truth of the answers we receive. Until this problem is rectified, the federal government is likely to be awash in federal contractors who are cheating on their taxes.

But there is good news to report as well. The principal objective of this Subcommittee’s investigation is to increase the effectiveness of the Federal Payment Levy Program under which a portion of federal contractor’s payments are levied to pay off their outstanding tax debt. When the Subcommittee started this investigation in 2003, levies on federal contractors amounted to \$7 million. In two short years, collections have grown to \$42 million. Substantial credit is due GAO and the Commissioner of IRS, the Administrator of GSA, the Secretary of Defense, and the Commissioner of the Financial Management Service whose support led to the establishment of the Federal Contractor Tax Compliance Task Force. The Task Force has addressed and resolved several problems that inhibit levies and it is continuing its work on a number of additional problems. I appreciate their hard work and I applaud their success.

To date, the notable accomplishments of these efforts include the establishment of a Taxpayer Identification Number Verification Program in the Central Contractor Registration, IRS’ release of \$28 billion in additional tax debt for levy purposes, and the creation and testing of a federal contractor non-filing program. All of these improvements are designed to increase the number of levies on federal contractors’ payments and the results demonstrate that we are succeeding.

But the Task Force’s work is not finished. The Financial Management Service must find ways to impose levies on all federal contractor payments, especially those that are made with

purchase cards. The Task Force needs to develop procedures to ensure that all federal contractors are registered in the Central Contractor Registration. Further, the Task Force needs to develop procedures to ensure that all federal agencies use the validated name and Taxpayer Identification Number from the Central Contractor Registration for all tax-related purposes. I expect that today's hearing will add to the Task Force's to-do list. Specifically, the tax-related questions in the Representations and Certifications Application need to be revised, and processes need to be developed to verify contractors' tax-related statements.

On the first panel this morning, we will hear from GAO representatives on the results of our request to determine if there are tax-delinquent federal contractors working for the General Services Administration or who are on GSA's General Schedule. To date, their hard work has resulted in the identification of 57,000 federal contractors who owe \$6.3 billion in unpaid taxes, including 97 contractors who had flagrantly abused the tax system and have been referred to IRS for further investigation.

On the second panel, we will hear from the Commissioner of IRS and the Acting Administrator of GSA concerning the actions they have taken or plan to take to ensure that federal contractors who abuse the tax system are identified and that those who owe tax have their contract payments levied. I would like to make it clear that I am pleased with the results that the Federal Contractor Tax Compliance Task Force has achieved to date. I applaud the Commissioner of IRS, the Administrator of GSA and other participants for their active support of the Task Force's work. However, I am concerned that only one of the 97 cases of potential fraud identified by this Subcommittee has been prosecuted. This is well below the infamous baseball Mendoza line.

In closing, it is simply unacceptable that tax cheats who owe the government millions in back taxes get millions of dollars from the government. This Subcommittee will continue to aggressively pursue this matter until the federal government tightens its procedures to ensure that these tax deadbeats are prohibited from receiving lucrative government contracts.

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